

# 3 FOR '21: KEY FIXED INCOME THEMES FOR THE NEW YEAR

Kevin Flanagan — Head of Fixed Income Strategy

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"3 for 21" would not be an ideal stat in the sporting world. But for fixed income investors, we feel three will be an important number in 2021, as, in our opinion, it represents the number of [key themes to focus on in the new year](#). Here's a brief synopsis of these themes and how WisdomTree can help provide solutions for them in the fixed income universe.

## 1. Quality and Income

With interest rates at historical lows, investors will be tasked with looking for income without moving too far out in [duration](#) or, perhaps more importantly, sacrificing credit quality.

- The [WisdomTree Yield Enhanced U.S. Aggregate Bond Fund \(AGGY\)](#) offers investors just such a strategy. This fund re-weights the sectors of the [Bloomberg Barclays U.S. Aggregate Bond Index \(Agg\)](#) utilizing important guardrails to enhance [yield](#) while maintaining a familiar risk profile. This approach focuses on the [investment-grade](#) aspect while keeping away from high yield, emerging market debt and/or leverage, a desirable trait for core fixed income.
- The [WisdomTree U.S. High Yield Corporate Bond Fund \(WHY\)](#) offers investors a quality screen while tilting for income. By focusing on only public issuers and their attendant [balance sheets](#), we were able to identify "[cash flow](#)" as a vital attribute. We eliminate those issuers with negative cash flow, helping to address credit quality concerns and potentially mitigating default risk.

## 2. Reflation Trade

While we expect the [Federal Reserve \(Fed\)](#) to keep rates at or near zero, intermediate to longer-dated [Treasury](#) yields could still grind higher, with the [yield curve](#) steepening due to unprecedented monetary and fiscal stimulus. Key factors such as pent-up demand and optimism surrounding the vaccine rollout could push inflation expectations and headline inflation readings higher in 2021.

- The [WisdomTree Interest Rate Hedged High Yield Bond Fund \(HYZD\)](#) offers investors a way to provide income while mitigating interest rate risk. This strategy utilizes our quality-screened high-yield approach while "zeroing" out duration. Thus, investors can address both income needs and rate concerns in just one Fund.
- The [WisdomTree Floating Rate Treasury Fund \(USFR\)](#) offers investors a rate-hedge strategy that focuses only on U.S. government securities and doesn't include any credit issuers, unlike most, if not all, other existing [floating rate](#) options. This approach also offers an attractive alternative to [inflation-protected securities](#) without the longer duration they typically include.

## 3. Emerging Markets

With the global economic setting expected to improve after Q1 2021, accommodative central bank policies in both the developed and emerging market worlds and the potential for a softer U.S. dollar setting, we anticipate a favorable setting for [local currency sovereign](#) emerging market debt (EMD).

- The [WisdomTree Emerging Markets Local Debt Fund \(ELD\)](#) offers investors an approach to take advantage of the potential opportunities in the local currency EMD space while utilizing a process of continuous risk management. Key factors in the risk-monitoring process include growth/inflation indicators, debt service capability and short-term [liquidity](#) factors, enabling countries that exhibit fiscal/monetary discipline to receive an increase in their respective allocation.

**On a final note:** Happy Holidays!

**Important Risks Related to this Article**

There are risks associated with investing, including possible loss of principal. High-yield or “junk” bonds have lower credit ratings and involve a greater risk to principal. Fixed income investments are subject to interest rate risk; their value will normally decline as interest rates rise. HYZD seeks to mitigate interest rate risk by taking short positions in U.S. Treasuries (or futures providing exposure to U.S. Treasuries), but there is no guarantee this will be achieved. Derivative investments can be volatile, and these investments may be less liquid than other securities, and more sensitive to the effects of varied economic conditions.

Fixed income investments are also subject to credit risk, the risk that the issuer of a bond will fail to pay interest and principal in a timely manner, or that negative perceptions of the issuer’s ability to make such payments will cause the price of that bond to decline. HYZD may engage in “short sale” transactions where losses may be exaggerated, potentially losing more money than the actual cost of the investment, and the third party to the short sale may fail to honor its contract terms, causing a loss to the Fund. While the Fund attempts to limit credit and counterparty exposure, the value of an investment in the Fund may change quickly and without warning in response to issuer or counterparty defaults and changes in the credit ratings of the Fund’s portfolio investments.

Securities with floating rates can be less sensitive to interest rate changes than securities with fixed interest rates, but may decline in value. The issuance of floating rate notes by the U.S. Treasury is new, and the amount of supply will be limited. The value of an investment in USFR may change quickly and without warning in response to issuer or counterparty defaults and changes in the credit ratings of the Fund’s portfolio investments.

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Foreign investing involves special risks, such as risk of loss from currency fluctuation or political or economic uncertainty. Investments in emerging, offshore or frontier markets are generally less liquid and less efficient than investments in developed markets and are subject to additional risks, such as risks of adverse governmental regulation and intervention or political developments. Investing in mortgage- and asset-backed securities involves interest rate, credit, valuation, extension and liquidity risks and the risk that payments on the underlying assets are delayed, prepaid, subordinated or defaulted on. Unlike typical exchange-traded funds, there is no index that ELD attempts to track or replicate. Thus, the ability of the Fund to achieve its objective will depend on the effectiveness of the portfolio manager. Due to the investment strategies of ELD, USFR, HYZD and AGGY, they may make higher capital gain distributions than other ETFs.

Please read each Fund’s prospectus for specific details regarding the Fund’s risk profile.

For standardized performance and the most recent month-end performance click [here](#) NOTE, this material is intended for electronic use only. Individuals who intend to print and physically deliver to an investor must print the monthly performance report to accompany this blog.

For more investing insights, check out our [Economic & Market Outlook](#)

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You cannot invest directly in an index.

## **DEFINITIONS**

**Duration** : A measure of a bond's sensitivity to changes in interest rates. The weighted average accounts for the various durations of the bonds purchased as well as the proportion of the total government bond portfolio that they make up.

**Bloomberg U.S. Aggregate Bond Index** : Represents the investment-grade, U.S. dollar-denominated, fixed-rate taxable bond market, including Treasuries, government-related and corporate securities, as well as mortgage and asset backed securities.

**Yield** : The income return on an investment. Refers to the interest or dividends received from a security that is typically expressed annually as a percentage of the market or face value.

**Investment grade** : An investment grade is a rating that signifies a municipal or corporate bond presents a relatively low risk of default.

**Balance sheet** : refers to the cash and cash equivalents part of the Current Assets on a firms balance sheet and cash available for purchasing new position.

**Cash flows** : a measure of how much cash a business generates after taking into account all the necessary expenses, including net capital expenditures.

**Reflation** : The term is used to describe the first phase of economic recovery after a period of contraction. This period is typically characterized by the act of stimulating the economy through accommodative central bank policies and reducing taxes, to bring growth and inflation back up to the long-term trend.

**Federal Reserve** : The Federal Reserve System is the central banking system of the United States.

**Treasury** : Debt obligation issued by the U.S. government with payments of principal and interest backed by the full faith and credit of the U.S. government.

**Yield curve** : Graphical Depiction of interest rates on government bonds, with the current yield on the vertical axis and the years to maturity on the horizontal axis.

**Floating Rate Treasury Note** : a debt instrument issued by the U.S. government whose coupon payments are linked to the 13-week Treasury bill auction rate.

**Treasury Inflation-Protected Securities (TIPS)** : Bonds issued by the U.S. government. TIPS provide protection against inflation. The principal of a TIPS increases with inflation and decreases with deflation, as measured by the Consumer Price Index. When a TIPS matures, you are paid the adjusted principal or original principal, whichever is greater.

**Local currency sovereigns** : debt denominated in local currencies issued by an emerging market government.

**Liquidity** : The degree to which an asset or security can be bought or sold in the market without affecting the asset's price. Liquidity is characterized by a high level of trading activity. Assets that can be easily bought or sold are known as liquid asset.